



DEPARTMENT OF
FINANCE

ARNOLD SCHWARZENEGGER, GOVERNOR

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May 14, 2010

Ms. Susan Sims, Chief Deputy Director
California Department of Water Resources
P.O. Box 942836, Room 1115-1
Sacramento, CA 94236-0001

Dear Ms. Sims:

Final Report—City of Crescent City, Infrastructure Rehabilitation Proposition 13 Grant Audit

The Department of Finance, Office of State Audits and Evaluations (Finance), has completed its audit of the City of Crescent City's (City) Proposition 13 grant agreement E68007 for the period June 10, 2004 through March 31, 2007.

The enclosed report is for your information and use. The City's response to the report findings are incorporated into this final report. The City agreed with our observations, and we appreciate its willingness to implement corrective actions. The observations in our report are intended to assist management in improving the effectiveness and efficiency of its operations.

In accordance with Finance's policy of increased transparency, this report will be placed on our website. Additionally, pursuant to Executive Order S-20-09, please post this report in its entirety to the Reporting Government Transparency website at <http://www.reportingtransparency.ca.gov/> within five working days of this transmittal.

We appreciate the assistance and cooperation of the City. If you have any questions regarding this report, please contact Frances Parmelee, Manager, or Rich Hebert, Supervisor, at (916) 322-2985.

Sincerely,

David Botelho, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: On following page

cc: Mr. James Barnts, Director of Public Works, City of Crescent City
Ms. Perla Netto-Brown, Controller, California Department of Water Resources
Mr. Jim Libonati, Deputy Director, California Department of Water Resources
Mr. Jeffrey Ingles, Chief Auditor, California Department of Water Resources
Ms. Tracie Billington, Chief, Special Projects Section, California Department of
Water Resources
Ms. Gail Chong, Chief, Bond Accountability Office, California Department of
Water Resources
Mr. Eric Koch, Chief, Flood SAFE Program Management Office, Division of Flood
Management, California Department of Water Resources
Mr. Eric Hong, Supervising Engineer, California Department of Water Resources
Mr. Patrick Kemp, Assistant Secretary for Administration and Finance, California Natural
Resources Agency
Mr. Bryan Cash, Deputy Assistant Secretary, California Natural Resources Agency
Ms. Julie Alvis, Deputy Assistant Secretary, California Natural Resources Agency

A GRANT AUDIT

City of Crescent City
Proposition 13 Bond Program
Grant Agreement E68007



Prepared By:
Office of State Audits and Evaluations
Department of Finance

MEMBERS OF THE TEAM

Frances Parmelee, CPA
Manager

Rich Hebert
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Final reports are available on our website at <http://www.dof.ca.gov>

You can contact our office at:

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BACKGROUND, SCOPE, AND METHODOLOGY

BACKGROUND

In March 2000, voters approved the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Act (Proposition 13), which authorized the State of California to sell \$1.97 billion in general obligation bonds. The bond proceeds provide funds for safe drinking water, water quality, food protection, and water reliability programs. Proposition 13 also provides funding for the protection, restoration, and interpretation of the diverse cultural influence and extraordinary human achievements that have contributed to the unique development of California.

The California Department of Water Resources (DWR) is one of many state departments that administer Proposition 13 programs and award funds in the form of grants. One of the programs—the Infrastructure Rehabilitation Program—provides funding to local public agencies and incorporated mutual water companies to improve or replace outdated, obsolete, or inefficient water lines. The program's goal is to improve water flow and quality, and to reduce the levels of rust and other particulate matter impairing public water supplies.

DWR awarded the City of Crescent City (City) a \$661,300 Proposition 13 grant to replace 4,500 linear feet of its undersize and aging water lines located in one of the City's older neighborhoods. The water lines in this neighborhood consisted of one inch pipes over 80 years old. Because these water lines had become badly rusted and obsolete, the water pressure was inadequate to meet peak demand. By replacing these obsolete lines, hydrants, and connectors with more modern and efficient equipment, the City will be able to provide better service at a lower cost for its customers.

SCOPE

In accordance with the Department of Finance's (Finance) bond oversight responsibilities, Finance conducted an audit of the City's Proposition 13 grant agreement E68007 for the period June 10, 2004 through March 31, 2007.

The audit objective was to determine whether the City's grant expenditures were in compliance with applicable laws, regulations, and grant requirements. In order to design adequate procedures to evaluate fiscal compliance, we obtained an understanding of the relevant internal controls. We did not assess the efficiency or effectiveness of program operations.

City management is responsible for ensuring accurate financial reporting and compliance with applicable laws, regulations, and grant requirements as well as evaluating the efficiency and effectiveness of the program. DWR along with the California Natural Resources Agency are responsible for state-level administration of the bond programs.

METHODOLOGY

To determine whether grant expenditures were in compliance with applicable laws, regulations, and grant requirements, we performed the following procedures:

- Interviewed key personnel to obtain an understanding of the grant-related internal controls.
- Examined the grant files maintained by DWR, the grant agreement, and applicable policies and procedures.
- Reviewed the City's accounting records, vendor invoices, warrants, and bank statements.
- Selected a sample of expenditures to determine if costs were allowable, grant-related, incurred within the grant period, supported by accounting records, and properly recorded.
- Performed procedures to determine if other revenue sources were used to reimburse expenditures already reimbursed with grant funds.
- Conducted a site visit to verify project existence.

The results of the audit are based on our review of documentation and other information made available to us by the City, and through interviews with the staff directly responsible for administering bond funds. The audit was conducted from July 2009 through March 2010.

This audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our observations and recommendations based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our observations and recommendations.

Except as noted below, the City of Crescent City (City) complied with applicable laws, regulations, and the grant requirements. While the audit did not result in questioned costs, one observation was identified as reported below. The Schedule of Claimed, Audited, and Questioned Amounts is presented in Table 1.

Table 1: Schedule of Claimed, Audited, and Questioned Amounts

Grant Agreement E68007 For the Period June 10, 2004 through March 31, 2007			
Category	Claimed	Audited	Questioned
Consulting and Engineering	\$169,755	\$169,755	\$ 0
Construction	477,540	477,540	0
Administrative & Management	7,646	7,646	0
Total Expenditures	\$654,941	\$654,941	\$ 0

Observation 1: Non-Compliance with Contract Provisions

The City entered into a contract with an engineering consulting firm and did not enforce certain contract provisions. Such provisions provide assurance that grant funds are used for intended purposes, and the project is completed within scope and cost. Specifically, we identified the following:

- *Non-Compliance with Budget Monitoring Requirements.* The contract required the consulting firm to establish and monitor costs using 11 budget categories. However, the firm collapsed the 11 categories and only used 2: (1) Design, Reporting, and Administration, and (2) Construction Inspection and Management.

The City accepted the consulting firm's cost reports because it was unaware of the required 11 budget categories. By not adhering to the agreed-upon budget categories, cost accountability and project monitoring was impaired.

The contract states the project consultant shall provide detailed task descriptions which provide a meaningful record to an independent auditor reviewing the task description. All invoices must be itemized, and must state such services were actually performed. Overly generalized listings of task descriptions are not acceptable.

- *Payment Retention Not Withheld.* Although not explicitly stated in the contract, Article A-5(a) of the grant agreement between DWR and the City states the local agency shall hold retention of not less than 10 percent from any contractor or combination of contracts until the project or any component of the contract is determined to be completed. Because the consulting firm is stepping into the shoes of the City, grant agreement provisions apply. We determined the City did not withhold 10 percent of the total contract amount from the consulting firm. By not withholding retention, the City limits its ability to remedy contractor non-performance.

Recommendation:

For future grants, the City should hold contractors accountable for complying with the contract provisions.

R_{RESPONSE}



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April 28, 2010

Department of Finance
Office of State Audits and Evaluations
300 Capital Mall, Suite 801
Sacramento, CA 95814

Subject: Letter dated April 22, 2010 with Draft Report – City of Crescent City, Infrastructure Rehabilitation Proposition 13 Grant Audit

This letter is written in response to the Draft Report prepared by the Office of State Audits and Evaluations, Department of Finance. The City of Crescent City is committed to complying with all of the grant contract provisions in the future. We wish to express our sincere pledge to provide the needed oversight of any future grants.

The scope and magnitude of the project the city was able to complete due to Proposition 13 was extremely beneficial to the community of Crescent City. We appreciate the work of the audit team and again reiterate our commitment to provide the needed oversight and to hold the contractors accountable for complying with contract provisions.

Sincerely,

A handwritten signature in blue ink, appearing to read "Jim Barnts", is written over a horizontal line.

Jim Barnts
Director of Public Works

JB:lj